

BACKLASH AGAINST ISDS

A CASE FOR A SUSTAINABLE DEVELOPMENT APPROACH TO INVESTMENT ARBITRATION FOR DEVELOPING COUNTRIES

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Abstract

Over the years, Investor-State Dispute Settlement (ISDS) has spurred a lot of controversies on its legitimacy and integrity. The criticisms mainly stem from the obscuring effect of ISDS on legitimate government regulation and the adventurist manner in which arbitral tribunals interpret substantive rights favouring foreign investors. This, in turn, has resulted in a backlash by States which is illustrated through various forms ranging from withdrawal from traditional Bilateral Investment Treaties (BITs), the development of new era BITs, to extremities of eliminating ISDS all-together. Although there are plausible reforms that have been adopted, the system is still a work in progress. Mechanisms must be incorporated to strike a balance between promotion and protection of investment and the sovereign right of the State to regulate investment in the public interest. Innovation and the adoption of regulatory tools that meet individual States developmental needs will play a focal role in attaining a comprehensive International Investment Agreements (IIAs) reform.

This paper argues that a paradigm shift from the competing interests of States and investors to a sustainable development approach will achieve a necessary balance in ISDS taking into account the interests of all stakeholders involved in investment arbitration.

Keywords: Investor-State Dispute Settlement, Promotion and Protection of Investment, International Investment Agreements, Bilateral Investment Agreements, Sustainable Development

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1.0 Introduction

The period between 1990 – 2007 saw a proliferation of Bilateral Investment Treaties (BITs): over 2500 BITs were signed between States¹ with capital exporting countries signing such BITs mainly for the protection of their investors abroad while capital importing countries doing so to attract foreign investments. However, with the boom in BITs, disputes unavoidably arose out of the agreements. The number of claims brought against States has continued to rise and being mostly on the losing end, States have had to pay numerous in compensation. As a result, the investment arbitration regime has been perceived by States as being pro-investor.²

The lack of predictability and coherence in decisions on significant political and economic matters and the lack of sustainability of the system as a whole in terms of promotion and protection of investments has, inevitably, led to the legitimacy deficit or what is referred to as a ‘legitimacy crisis’ in international investment arbitration.³ This has resulted in a backlash by States against the system. The backlash is illustrated through various forms ranging from withdrawal from traditional BITs,⁴ the development of new era BITs,⁵ to extremities of eliminating ISDS all-together.⁶ In addition, a number of Latin American States have recently withdrawn from the International Centre for Settlement of Investment Disputes (ICSID) Convention⁷ while others, for instance, Australia, have refrained from including ISDS in new International Investment Agreements (IIAs).⁸

¹ UNCTAD, ‘The Entry into Force of Bilateral Investment Treaties (BITs)’ IIA Monitor No. 3 (2006) International Investment Agreements, available at https://unctad.org/en/Docs/webite-ia20069_en.pdf, accessed 11 Dec 2018.

² Stephan W. Schill, ‘Reforming Investor-State Dispute Settlement: A Comparative and International Constitutional Law Framework’ (2017) 20 *Journal of International Economic Law* 649.

³ See generally, M Sornarajah, *Resistance and Change in the International Law on Foreign Investment*, (Cambridge University Press, 2015).

⁴ Ecuador has terminated twelve investment treaties, withdrawal from ICSID Convention and notification of revision of 24 BITs. See also UNCTAD Report (2017), Phase 2 of IIA Reform: Modernizing The Existing Stock of Old-Generation Treaties, “of 212 BITs terminated as of March 2017, 19 treaties (9 per cent) were jointly terminated, without any replacement or consolidation; another 59 (28 per cent) were unilaterally terminated, while 134 (63 per cent) were replaced by a new treaty”, available at https://unctad.org/en/PublicationsLibrary/diaepcb2017d3_en.pdf.

⁵ Ibid.

⁶ See for instance, South Africa.

⁷ UNCTAD Report 2017, *supra* n 4.

⁸ Vera Korzun, ‘The Right to Regulate in Investor-State Arbitration: Slicing and Dicing Regulatory Carve-Outs’ (2016) 50 *Vanderbilt Journal of Transnational Law* 355.

In addition to the backlash by States, international organisations, in particular United Nations Conference on Trade and Development (UNCTAD), have been very vocal regarding the current IIA regime.⁹ UNCTAD has identified key areas for reform, in particular, the policy objectives of safeguarding the right to regulate, reforming ISDS, promoting and facilitating investment and ensuring responsible investment.

It is worth noting that the backlash by States and other international organisations against the current IIA regime and the reforms underway are geared towards not only protection and promotion of foreign investments, but also compatibility with sustainable development. In fact, it is safe to say that, investment protection is enmeshed with the achievement of sustainable development goals. As noted in UNCTAD's 2016 *World Investment Report*, '[r]eform to bring the IIA regime in line with today's sustainable development imperative is well underway. Today, the question is not about whether to reform, but about the what, how and extent of such reform'.¹⁰

There are plausible reforms that have been adopted so far. However, the system is still a work in progress.¹¹ Innovation and the adoption of regulatory tools that meet individual State's developmental needs will play a focal role in attaining a comprehensive IIA reform. This paper argues that a paradigm shift from the competing interests of States and investors to a sustainable development approach will help achieve the necessary balance in ISDS taking into account the interests of all stakeholders involved.

This paper is divided into four main parts: the first part provides a general introduction to the issues under discussion. The second part will problematise the regime of ISDS from the perspective of developing countries in order to lay the basis for core arguments that will be developed later. The third part will do an appraisal of some approaches that countries have proposed or have employed as alternatives to the current ISDS system. Mainly, this paper will assess the case of South Africa, Brazil and India. Finally, the fourth part will make a case for a sustainable development approach in ISDS.

⁹ United Nations Conference on Trade and Development has published numerous literature on the current investment regime.

¹⁰ UNCTAD, *World Investment Report 2016, Investor Nationality: Policy Challenges* (United Nations, New York and Geneva 2016) 108, available at https://unctad.org/en/PublicationsLibrary/wir2016_en.pdf, accessed 18 April 2019.

¹¹ Ibid.

2.0 ISDS: A Troubled Regime

The contemporary ISDS regime has generated a lot of debate among scholars of international investment law. For the proponents of the system, it is argued that ISDS is the most effective mechanism for the protection of foreign investments and to ensure that States are held accountable for government conduct affecting such investments either directly or indirectly.¹² Among the critics, the expansionary and adventurist manner in which arbitral tribunals interpret treaty provisions is pro-investor and this forms the underlying basis of the legitimacy crisis in ISDS.¹³ In this context, the inclination towards pro-investor interpretations is based upon the ideology that such standards of investment protection are necessary for the promotion of investment inflows and ultimately economic development of the host State. Even though it has been argued that this is the root cause of the ISDS legitimacy crisis, this paper seeks to explore a nuanced approach to the root cause in the context of developing countries.

Upon attaining independence, most developing countries were left economically crippled and in desperation for investment in-flows so as to boost and place their economies into the global commons. During this time, most countries were seeking ways to attract all forms of investments. Coupled with the perception that developing countries had weak justice systems and were prone to political instability, most IIAs arising from this epoch were drafted with the protection of investors and their investments in mind while significantly undermining States' rights on regulation and overall protection of their citizens on matters pertaining human rights, sustainable development and environmental standards. In this race to the bottom, viewed from the perspective of public interest, very weak agreements ensued. In addition, factors such as corruption, a glaring menace in developing countries, lack of adequate expertise in the negotiation of investment treaties and ignorance of the ultimate rights being given up, further weakened the position of developing countries in investment relations. This was the 'original sin.'

Over the years, the ISDS regime has spurred a lot of controversies on its legitimacy and integrity which have revolved around five main issues.

First, it has been contended that the system exhibits bias in favour of investors by granting them expansive rights while failing to adequately

¹² Schill, *supra* n 2.

¹³ M Sornarajah, *supra* n 3 at 451.

address the rights of host States, mainly in terms of government regulation for the public interest.¹⁴ This issue concerns both the obscuring effect of ISDS on government regulation and the adventurist nature of interpretations of substantive rights by arbitral tribunals favouring foreign investors.

On the effect of ISDS on government regulation, it has been argued that this stems from the fact that States have broad obligations under investment agreements, such that, any legitimate government regulation in the interest of the public affecting investments either directly or indirectly, can be subject to investment arbitration.¹⁵ This observation explains why most cases before arbitral tribunals concern government regulation.¹⁶ Moreover, tribunals are in the habit of looking into the extent to which a regulation affects an investor rather than looking at the overall purpose of a regulation or a government measure.¹⁷ This kind of reasoning has a direct effect on States in terms of regulation for the public interest and can potentially result in a regulatory chill where States opt to avoid regulating or simply not regulate to the extent they should in matters of public welfare such as health, safety and environmental standards.¹⁸ In addition, arbitral tribunals have also been criticised on the innovative and broad manner in which they interpret substantive rights solely for the benefit of foreign investors.¹⁹ This further curtails a host State's roles of exercising its regulatory function in the public interest.

¹⁴ M Sornarajah, supra n 3; Aaron Cosby, 'The Road to Hell? Investor Protections in Nafta's Chapter 11' in Lyuba Zarsky (ed), *International Investment for Sustainable Development: Balancing Rights and Rewards*, (Monetary Institute for International Studies 2005), Frank Emmert and Begaiym Esenkulova, 'Balancing Investor Protection and Sustainable Development in Investment Arbitration – Trying to Square the Circle?' available https://www.researchgate.net/publication/327729018_Balancing_Investor_Protection_and_Sustainable_Development_in_Investment_Arbitration_-_Trying_to_Square_the_Circle, accessed 15 December 2018.

¹⁵ Ibid, Emmert and Esenkulova.

¹⁶ Lisa Diependaele, Ferdi De Ville & Sigrid Sterckx 'Assessing the Normative Legitimacy of Investment Arbitration: The EU's Investment Court System' (2019) 24 (1) *New Political Economy*, 37.

¹⁷ Ibid.

¹⁸ See, however, Giovanni Zarra, 'Right to Regulate, Margin of Appreciation and Proportionality: Current Status in Investment Arbitration in Light of Philip Morris v. Uruguay' (2017) 14 (2) *Brazilian Journal of International Law*, 95 who argues that, on a positive note, tribunals are seen to react to this criticism and embracing the notion of putting due weight on the purpose of the government measure rather than just the negative effects of the regulation on investments.

¹⁹ For instance, the broad manner in which arbitral tribunals have interpreted legitimate expectation, FET, FPS. See, for example, in *Railroad Development Corporation (RDC) v Republic of Guatemala*, ICSID Case No. ARB/07/23, Award, where the arbitral tribunal rejected the argument to link the FET standard to state practice and opinion juris, which is a more restrictive standard, this broad interpretation of FET is also evidenced in *Waste Management v United Mexican States* (II), ICSID Case No. ARB (AF)/00/3.

Second, there is unpredictability and lack of coherence in decisions. Consistency and coherence in decisions are the cornerstone of any legal system. Arbitral tribunals are increasingly rendering conflicting decisions on cases involving similar issues²⁰ and at times even arising out of the same IIA. A notable example of this situation is the *SD Meyers v Canada*²¹ case and the *Metalclad v Mexico*²² case where the respective tribunals adopted different interpretation for fair and equitable treatment arising out of the same treaty, i.e. NAFTA. The inconsistency in decisions, especially seeing that such decisions are mainly on public issues that have significant financial and political implications, is a major blow to the ISDS regime. As aptly argued, ‘...the mantra of one case not being binding on any other, each one being an individual, one-off, ad-hoc process, has no place in a legal system that passes judgment on a vast range of government measures affecting international investments’.²³ It has been suggested that a well-established appellate court system could be the way forward to cure such inconsistencies and to enhance predictability and coherence in decision making.²⁴ Sornarajah, on the other hand, argues that an appellate facility would merely be, ‘a superstructure built onto the rotten foundations of the existing system’.²⁵ He suggests ‘wiping the slate clean’ as the ultimate solution in ISDS. This argument, although theoretically appealing, as Lim et al. note, the global political will required for starting on a clean slate is lacking especially in light of the reforms that have been introduced in the system.²⁶ Given that under the current ISDS regime, there is no system of precedence and each case is decided as a stand-alone, ad-hoc process, an appellate court may present a good avenue to cure the system of the criticisms of inconsistency and unpredictability.

²⁰ See for instance the *Lauder* cases, *CME Czech Republic B.V. v Czech Republic*, Ad hoc – UNCITRAL Arbitration Rules, Partial Award of 13 September 2001, Final Award of 14 March 2003; and *Lauder v Czech Republic*, Final Award, 3 September 2001, Ad hoc - UNCITRAL Arbitration Rules.

²¹ *SD Meyers Inc. v Canada*, 2000.

²² *Metalclad Corporation v United Mexican States* (2000). ICSID Case No. ARB(AF)/97/ 1 (2000).

²³ Mann, H. et al. *Comments on ICSID Discussion Paper, ‘Possible Improvements of the Framework for ICSID Arbitration’* International Institute for Sustainable Development (IND), 2004, 6.

²⁴ Juan Pablo Charris Benedetti, ‘The Proposed Investment Court System: Does It Really Solve the Problems’, (2019) 42 *Review Derecho del Estado* 83.

²⁵ M. Sornarajah *supra* n 3.

²⁶ Chin Leng Lim, Jean Ho & Martins Paparinskis, *International Investment Law and Arbitration: Commentary, Awards and other Materials*, (Cambridge: Cambridge University Press, 2018) 73.

Third, the cost of investment arbitration has been perceived as being high.²⁷ Costs incurred in investment arbitration are quite substantial.²⁸ Empirical studies show that even partial costs could represent up to more than 10% of the total arbitration award.²⁹ This coupled with the inconsistencies and unpredictability in awarding costs,³⁰ further escalates the controversies surrounding ISDS.

Fourth, the credibility of arbitrators is a rising concern among States, especially, on the so-called role-issue conflict where an arbitrator would also be an investment lawyer. As such, they may have to decide on a particular issue where they may also potentially have to advise and represent clients concerning the same issue. A conflict of interest is inevitable and the perception of impartiality and neutrality is, thus, compromised. In addition, it has been argued that there is insufficient attention on arbitrators' qualification. Procedural frameworks and IIAs are normally silent on substantive requirements regarding qualifications of arbitrators.³¹ For instance, the ICSID Convention merely provides that arbitrators should be 'of high moral character and [have] competence in the field of law, commerce, industry, or finance and may be relied upon to exercise independent judgement.'³² United Nations Commission on International Trade Law (UNCITRAL) Rules only require the arbitrators to disclose circumstances that would raise doubts regarding their impartiality.³³ However, some new era treaties address this issue and prescribe precise qualifications to be held by arbitrators should a dispute ensue.³⁴

Finally, the lack of transparency and the lack of sufficient representation of the public in matters that generate great public interest further exacerbate the problems of ISDS. ISDS still remains a closed system of dispute settlement with disputes mainly decided behind closed doors. Non-disputing

²⁷ See Susan D Frank, 'Rationalizing Costs in Investment Treaty Arbitration' (2011) 88(4) Washington University Law Review 769.

²⁸ See, for instance, *Yukos Universal Limited (Isle of Man) v The Russian Federation*, UNCITRAL, PCA Case No. AA 227, Yukos tribunal ordered Russia to pay \$60 million in legal fees to Yukos lawyers.

²⁹ Ibid.

³⁰ Emmert and Esenkulova supra n 14.

³¹ Lisa Diependaele et al, supra n 16.

³² ICSID Convention, Article 14.

³³ UNCITRAL, Article 11.

³⁴ See for instance, Transatlantic Trade and Investment Partnership, EU-Canada Comprehensive Economic and Trade Agreement.

parties, under the current ISDS regime, have no legal rights to participate or influence the outcomes of the disputes.³⁵ Amicus briefs still remain a rarity in ISDS.³⁶ Investments and even investment disputes have social, economic and political impacts on the local communities of a host State and exclusion of these communities, especially from dispute settlement, effectively shuts out their experiences. As noted, the bulk of ISDS cases arise out of governmental regulations and measures on public policy challenged by investors. In fact, even legitimate measures of the host State on environmental and health regulation, affecting investments either directly or indirectly can be challenged before an arbitral tribunal. For instance, in the *Philip Morris* case,³⁷ Philip Morris sued Uruguay and Australia for their requirements for health warnings on cigarette packets. In *Vattenfall* case,³⁸ a Swedish energy company, sued Germany for regulations phasing out nuclear energy and similarly in *Methanex* case,³⁹ the extent to which a government may exercise its sovereign right to ban a potentially harmful substance to both health and the environment was challenged. As rightly noted, in these circumstances, the decisions of the tribunals will have ‘implications that go far beyond commercial impacts to such public policy objectives as the protection of the environment and public health and safety.’⁴⁰ Under all these circumstances, the resulting effect of the process is felt by more than just the parties involved.

3.0 Whither alternatives to ISDS?

The legitimacy crisis in the ISDS regime has resulted in a backlash by States against the system as noted in the introduction. Under this section, the paper will critically assess some approaches employed by States, in particular, States in the Global South, as alternatives to the current ISDS system. Mainly, the research will assess the case of South Africa, Brazil and India, especially because of the recent developments in their investment regimes and the possible

³⁵ Jandhyala, Srividya, ‘Why Do Countries Commit to ISDS for Disputes with Foreign Investors?’ (2016) 16 (1) A I B Insights; East Lansing, 7.

³⁶ Emmert and Esenkulova supra n 14.

³⁷ *Philip Morris Brands Sàrl, Philip Morris Products S.A. and Abal Hermanos S.A. v Oriental Republic of Uruguay*, ICSID Case No. ARB/10/7.

³⁸ *Vattenfall AB and Others v Federal Republic of Germany*, ICSID Case No. ARB/12/12.

³⁹ *Methanex Corporation v United States of America*, NAFTA/UCITRAL Award, 03/08/2005.

⁴⁰ Cosby, supra n 14.

impact that they could have in reshaping the current investment treaty system. In each of these cases, as will be discussed below, there are circumstances that have triggered and galvanised the policies adopted by the States.

3.1.0 South Africa

Like many other post-colonial States and after the end of its social, economic and political global isolation due to apartheid, South Africa got into a state of euphoria signing as many investment agreements as possible so as to attract Foreign Direct Investments (FDI) into its economy. This was confirmed by a study that concluded that, ‘...[i]n less than a decade, South Africa ha[d] become one of the top 10 investors in, and trading partner of, many African countries, displacing those companies from Europe (particularly in countries that were former colonial powers) and America, which ha[d] traditionally retained their economic links in Africa.’⁴¹

However, as with the conclusion of the BITs, disputes inevitably arose between the host State and the foreign investors. With each of these disputes, South Africa became more sceptical of the rights being given up by the State in the name of attracting FDI.⁴² This, especially, in terms of the sovereign rights of the State to regulate in the public interest. More so, this has to be seen in light of South Africa’s history of apartheid, the economic inequalities suffered during that period and its constitutional-based transformation agenda. Of significance, is the case of *Piero Foresti, Laura de Carli & Others v The Republic of South Africa* of 2007⁴³ which was the ultimate eye opener for South Africa. In this case, the Black Economic Empowerment policies (BEE), a crucial feature of South Africa’s National Development Plan, guaranteed under the Constitution as affirmative action measures whose mandate is to

⁴¹ D. Games, ‘The Experience of South African Firms in Doing Business in Africa: A Preliminary Survey and Analysis’ (2004) South African Institute for International Affairs, Business in Africa Research Project.

⁴² Sibanda Omphemetse S., ‘The Promotion and Protection of Foreign Investment Law Bill: Denunciation of BITs, and the De-internationalisation of Investor-State Arbitration in South Africa’ (2014) 4(4) London: The Academy of Business and Retail Management.

⁴³ *Piero Foresti, Laura de Carli & Others v The Republic of South Africa*, ICSID Case No. ARB (AF)/07/1

cure the lingering effects of the apartheid era,⁴⁴ was challenged as being contrary to the obligations of South Africa under the Italy-South Africa BIT.

Against this backdrop, the Government of South Africa began the process of reviewing its BITs and their impact on economic development and the sovereign right of the State to regulate.⁴⁵ Following this review, it was concluded that, ‘the current system [had] open[ed] the door for narrow commercial interests to subject matters of vital national interest to unpredictable international arbitration that may constitute direct challenges to legitimate, constitutional and democratic policy-making.’⁴⁶ Further, that the ‘Cabinet understood that the relationship between BITs and FDI was ambiguous at best, and that BITs pose risks and limitations on the ability of the Government to pursue its Constitutional-based transformation agenda. Cabinet concluded that South Africa should refrain from entering into BITs in future, except in cases of compelling economic and political circumstances.’⁴⁷ Following this, South Africa terminated several Bilateral Investment Treaties (BITs) to which it was a party.⁴⁸

Subsequently South Africa opted for a legislative approach in its investment relations and in 2013, South Africa published for public comment the Promotion and Protection of Investment Bill which was consequently enacted in 2015 as the Promotion of Investment Act 22 of 2015.⁴⁹

Of its striking features, the Act explicitly grants the South African Government the right to take regulatory measures in order to: redress historical, social and economic inequalities and injustices; uphold the rights, values and principles contained in the Constitution of the Republic of South Africa; and to promote and preserve cultural heritage, foster economic development, protect

⁴⁴ Elizabeth Whitsitt, An ICSID Tribunal Introduces Innovative Steps into Non-Disputing Party Procedure, *Investment Treaty News*, (10 October, 2009), available at <https://www.iisd.org/itn/2009/10/10/an-icsid-tribunal-introduces-innovative-steps-into-non-disputing-party-procedure/>.

⁴⁵ Tarcisio Gazzini, ‘Travelling the National Route: South Africa’s Protection of Investment Act 2015’ (2018) 26 (2) *African Journal of International and Comparative Law* 242.

⁴⁶ See Dr. Rob Davis, Minister of Trade and Industry, in his speech at the launch of UNCTAD’s Investment Policy Framework for Sustainable Development in Geneva in September 2012, available at <http://www.dti.gov.za/delegationspeechdetail.jsp?id=2506>.

⁴⁷ Minister of Trade and Industry, Dr. Rob Davis, in his speech at the launch of UNCTAD’s Investment Policy Framework for Sustainable Development in Geneva in September 2012.

⁴⁸ Gazzini, *supra* n 48.

⁴⁹ South Africa, Protection of Investment Act 2015 (Act 22 of 2015), *Government Gazette*, 606, 39514, 15 December 2015, available at http://www.gov.za/sites/www.gov.za/files/39514_Ac-22of2015ProtectionOfInvestmentAct.pdf, accessed on 28 December 2018.

the environment; and achieve the progressive realisation of socio-economic rights.⁵⁰ The Act also provides for investor protections: it provides *inter alia*, for national treatment,⁵¹ just and equitable compensation on expropriation,⁵² a physical security of property standard⁵³ and a right to transfer funds. It is interesting to note that on compensation for expropriation, the Act has shifted from the traditional rule of compensation of full market value to what is deemed to be just and equitable.

On dispute resolution, the Act is argued to be reminiscent of the Calvo doctrine,⁵⁴ and it provides for the settlement of investment disputes through the domestic justice system.⁵⁵ The Act further provides for international arbitration. However, it requires that the ‘arbitration will be conducted between the Republic and the home state of the applicable investor.’⁵⁶ The

⁵⁰ Richard Jansen van Vuuren, ‘Investment Laws in South Africa – Foreign Investors take Note’ [2018] Mining Review Africa, available at <https://www.miningreview.com/international/changes-investment-laws-south-africa-foreign-investors/>.

⁵¹ Section 8, South Africa Protection of Investment Act, 2015.

⁵² Section 10, Protection of Investment Act, 2015, reference is made to section 25 of the South African Constitution which in relation to expropriation provides:

25(2) Property may be expropriated only in terms of law of general application—

- (a) for a public purpose or in the public interest; and
- (b) subject to compensation, the amount of which and the time and manner of payment of which have either been agreed to by those affected or decided or approved by a court.

25(3) The amount of the compensation and the time and manner of payment must be just and equitable, reflecting an equitable balance between the public interest and the interests of those affected, having regard to all relevant circumstances, including—

- (a) the current use of the property;
- (b) the history of the acquisition and use of the property;
- (c) the market value of the property;
- (d) the extent of direct state investment and subsidy in the acquisition and beneficial capital improvement of the property; and
- (e) the purpose of the expropriation.

⁵³ Section 9, *Ibid*.

⁵⁴ Tarcisio Gazzini, ‘Travelling the National Route: South Africa’s Protection of Investment Act 2015’ (2018) 26(2) African Journal of International and Comparative Law 242, making reference to ‘calvo grandchildren’.

⁵⁵ Section 13(4): Subject to applicable legislation, an investor, upon becoming aware of a dispute as referred to in subsection (1), is not precluded from approaching any competent court, independent tribunal or statutory body within the Republic for the resolution of a dispute relating to an investment.

⁵⁶ *Ibid*, Section 13(5): The government may consent to international arbitration in respect of investments covered by this Act, subject to the exhaustion of domestic remedies. The consideration of a request for international arbitration will be subject to the administrative processes set out in section 6. Such arbitration will be conducted between the Republic and the home state of the applicable investor.

State-State arbitration can only be resorted to after exhaustion of domestic remedies. South Africa takes investment disputes back to the era of diplomatic protection where the home state would be invited to espouse a claim on behalf of its investor. This, as Kidane observes, is ‘reminiscent of the pre-BIT days of self-help and gunboat diplomacy.’⁵⁷ ISDS, as Echandi rightly observes, being rule-oriented, governed by principles and rules established by law, is instrumental in the elimination of politics and power-oriented diplomacy in international investment relations.⁵⁸ In addition, critics have argued that the Act seems to be leaning more towards the protection of public interest and significantly curtails investors’ protections as found in traditional BITs.⁵⁹

South Africa has taken a rather radical measure by eliminating ISDS. Even though ISDS has its weaknesses, it is the one innovation that has successfully governed international investment relations excluding interference through States politics, which the South African approach is prone to. In addition, the idea of espousal of claims by home States means that the investor will have limited access in terms of control and direction of the dispute. As Gazzini observes, ‘the entire proceedings and all decisions related to the dispute (including a possibly friendly settlement or an agreement on compensation) will be firmly in the hand of the home state with all the associated shortcomings and implications.’⁶⁰

⁵⁷ Won Kidane, ‘Contemporary International Investment Law Trends and Africa’s Dilemmas in the Draft Pan-African Investment Code’ (2018) 50 *The George Washington International Law Review Journal* 523.

⁵⁸ Roberto Echandi, ‘What do Developing Countries Expect from the International Investment Regime?’ in Jose E. Alvarez, Karl P. Sauvant, Kamil Girard Ahmed, and Gabriela P. Vizcamno, (eds), *The Evolving International Investment Regime: Expectations, Realities, Options*, (Oxford: Oxford University Press, 2011).

⁵⁹ Mmiselo Freedom Qumba, ‘Safeguarding Foreign Direct Investment in South Africa: Does the Protection of Investment Act Live up to its Name?’ (2018) 25 (3) *South African Journal of International Affairs* 341.

⁶⁰ Tarcisio Gazzini, ‘Travelling the National Route: South Africa’s Protection of Investment Act 2015’ (2018) 26(2) *African Journal of International and Comparative Law* 242. See also UNC-TAD Series on International Investment Agreements II, Investor-State Dispute Settlement: A Sequel, available at https://unctad.org/en/PublicationsLibrary/diaeia2013d2_en.pdf, accessed 5 January 2019.

3.2.0 Brazil

Out of the 2352 BITs in force signed between 1957 and 2019,⁶¹ none involves Brazil.⁶² It is worth noting that between 1994 and 1999, Brazil had actually signed 14 traditional BITs. However, none of them was approved by Congress⁶³ for granting excessive protection of private interests at the expense of government's regulatory flexibility. In addition, there was a general lack of trust on the capacity of BITs to attract investments in Brazil.⁶⁴

Despite having no BIT in force, Brazil continued to receive significant FDI inflows.⁶⁵ This reinforced the comprehension that investment inflows are not necessarily influenced by BITs in force.⁶⁶

However, having undergone political and economic transformations, Brazil's status, as mainly a capital importer, altered and it became an exporter of capital as well.⁶⁷ In fact, by the end of 2014, the stock of Brazilian FDI abroad corresponded to almost half of the amount of FDI in Brazil.⁶⁸ This coupled 'with the interest of partner countries in negotiating investment agreements, the several problems perceived in traditional BITs and the growing number of investor-state arbitration cases raised the debate of investment agreements again in Brazil.'⁶⁹

⁶¹ United Nations Conference on Trade and Development (UNCTAD), Investment Policy Hub, International Investment Agreements Navigator, available at <https://investmentpolicy.unctad.org/international-investment-agreements>, accessed 27 June 2019.

⁶² United Nations Conference on Trade and Development (UNCTAD). (2017). International investment agreements navigator available at <http://investmentpolicyhub.unctad.org/IIA>, accessed 23 April 2019.

⁶³ Ibid.

⁶⁴ For a detailed discussion on Brazil's resistance to traditional BITs, see Michelle Ratton Sanchez Badin and Fabio Morosini, 'Navigating between Resistance and Conformity with the International Investment Regime: The Brazilian Agreements on Cooperation and Facilitation of Investments (ACFIs)' in Fabio Morosini and Michelle Ratton Sanchez Badin (Eds), *Reconceptualizing International Investment Law from the Global South* (Cambridge: Cambridge University Press, 2018).

⁶⁵ UNCTAD *World Investment Report* (2016), supra n 10.

⁶⁶ José Henrique Vieira Martins, 'Brazil's Cooperation and Facilitation Investment Agreements (CFIA) and Recent Developments', (2017), available at <https://www.iisd.org/itn/2017/06/12/brazils-cooperation-facilitation-investment-agreements-cfia-recent-developments-jose-henrique-vieira-martins/>, accessed 20 April 2019.

⁶⁷ Brazilian Central Bank. (2014). *Brazilian Capital Abroad*, available at <http://www4.bcb.gov.br/rex/CBE/Ingl/CBE2014Results.pdf>, accessed 20 April 2019.

⁶⁸ Ibid.

⁶⁹ Ibid at 65.

These developments warranted a new plan of action for Brazil and acted as a platform for Brazil to exercise innovation in coming up with a model that would not only protect investments but also promote and facilitate productive investments. Brazil in 2015, thus, adopted a new approach: the Cooperation and Facilitation Investment Agreement (CFIA).

The model CFIA seeks to protect and promote investments as well as preserve Brazil's right to regulate in the public interest. Institutional governance, risk mitigation and thematic agendas for investment cooperation and facilitation form the substratum of the CFIA.⁷⁰

Undoubtedly impressive and innovative, risk mitigation and institutional governance aim at prevention of disputes and improvement of investment relations between the parties through the establishment of focal points such as ombudsmen to enhance dialogue between the parties.⁷¹ Like the South African Act, investor-state arbitration is eliminated and instead it provides for State-State arbitration. Other interesting innovations in the model include incorporation of corporate and social responsibility principles and clauses concerning corruption. In addition, CFIA's require investors to partake in the sustainable development of the host State and adherence to environmental protection standards and respect for human rights.⁷²

Among the strong points on the Brazil CFIA's, as has been observed by Hawes, is the promotion of amicable settlement of disputes before opting for a rather adversarial arbitration approach.⁷³ In addition, CFIA's expressly foster sustainable development for the Host State. Although traditional BITs are intended to promote this aspect as well, they are normally drafted with the protection of investment as a priority.

On the other hand, the negatives include the lack of mention of substantive provisions on fair and equitable treatment and indirect expropriation and the

⁷⁰ The Cooperation and Facilitation Investment Agreement, available at <http://www.mdic.gov.br/arquivos/CFIA-Presentation-EN.pdf>, accessed 5 January 2019.

⁷¹ Ibid.

⁷² Ibid.

⁷³ Stephanie Grace Hawes, 'Trends in Investment Treaty Arbitration: A Perspective on Brazil' (*Arbitration Blog*, 30 October 2017), available at <http://arbitrationblog.practicallaw.com/trends-in-investment-treaty-arbitration-a-perspective-on-brazil/>, accessed 20 December 2018; see also Vivian Gabriel, 'The New Brazilian Cooperation and Facilitation Investment Agreement: An Analysis of the Conflict Resolution Mechanism in Light of the Theory of the Shadow of the Law' (2016) 34(2) *Conflict Resolution Quarterly*, 141.

limitation of access to dispute resolution.⁷⁴ In addition, the proposed system of focal points has been criticised for limiting lodging of complaints to only the investors and the State since investments have social and economic impacts on the local community. As observed by Bernasconi-Osterwalder and Brauch,⁷⁵ the focal points should be expanded to accommodate concerns raised by all stakeholders involved including the members of the public. In addition, they argue that the system does not provide an avenue for public participation and accountability and, as such, is prone to corruption opportunities. On state-state arbitration, the system risks the same challenges as South Africa, as discussed above. The system is further criticised for not having a model text of the CFIA.⁷⁶ So far, CFIA's have varied depending on the counterparty of the agreement. This in turn will, no doubt, result in inconsistencies in the rather 'young' system. However, it has been observed that the lack of uniformity of the CFIA's is indicative of Brazil attempting to cater for the different needs of each partner and the possibility to continually improve the model.⁷⁷

Brazil's CFIA system is greatly inspired by the South Korea's success story of preventive dispute settlement. However, Brazil made a significant modification on the South Korea system and, instead of ISDS, it opted for State-State arbitration. This has serious consequences on the bargaining power of the parties. Under State-State arbitration, an investor is not assured that its home State will take up and pursue their claim. Therefore, investors have no leverage in the negotiations and hence lack incentive to partake in the preventive negotiations.⁷⁸ Nevertheless, it is yet to be seen how this regime will fair in the international investment regime. The incorporation of promotion of sustainable development and 'regulatory space' for the Host State are in no doubt a major plus for the Brazil CFIA. In addition, as observed, 'the positive

⁷⁴ See Ely Caetano Xavier Jr, José Augusto Fontoura Costa, 'Expropriation in Brazil's Cooperation and Facilitation Investment Agreements: A Failed Attempt to Think Outside the Box' (2017) *Yearbook on International Investment Law and Policy*, 444.

⁷⁵ Bernasconi-Osterwalder, Nathalie, and Martin Dietrich Brauch, 'Comparative Commentary to Brazil's Cooperation and Investment Facilitation Agreements (CIFAs) with Mozambique, Angola, Mexico, and Malawi' (2015) *International Institute for Sustainable Development*, available at <https://www.iisd.org/sites/default/files/publications/commentary-brazil-cifas-acfis-mozambique-angola-mexico-malawi.pdf>, accessed 29 December 2018.

⁷⁶ *Ibid.*

⁷⁷ *Supra* n 65.

⁷⁸ See Vivian Gabriel, 'The New Brazilian Cooperation and Facilitation Investment Agreement: An Analysis of the Conflict Resolution Mechanism in Light of the Theory of the Shadow of the Law' (2016) 34(2) *Conflict Resolution Quarterly*, 141.

repercussion of the model among relevant economic agents and partners, as well as in the international academic and cooperation circles, show that the model seems to be heading in the right way.⁷⁹

3.3.0 India

Until very recently, there was hardly any domestic discussion on India's approach to negotiating investment treaties. However, there are a series of developments that woke up India to the realities of investment treaty arbitration. There were three such developments.⁸⁰ First, up to 2010, there were barely any claims against India. This position changed and India increasingly found itself as a respondent in ISDS claims. In fact, it wasn't until 2011, that the first publicly known BIT arbitral award was issued against India in *White Industries v India*.⁸¹ After this award, the Government of India has received a series of notices of disputes from a number of foreign corporations (investors) challenging a wide array of regulatory measures taken by India, mainly, in the telecom industry following the cancellation of telecom licenses by the Indian Supreme Court in 2012.⁸²

The second development relates to the domestic pressures against the investment regime in India by different actors in academia, civil society organisations⁸³ and parliamentarians.⁸⁴ Following the *White Industries* case and the swelling number of ISDS notices against India, the demands for a crucial assessment of BITs in India only escalated.

Finally, there were internal discussions within the Indian Government on the urgent need to review its BITs. This is evidenced by the Ministry of

⁷⁹ Ibid.

⁸⁰ Prabhash Ranjan and P. Anand, 'The 2016 Model Indian Bilateral Investment Treaty: A Critical Deconstruction' (2017) 38 *Northwestern Journal of International Law & Business* 1.

⁸¹ *White Industries Australia Limited v. Republic of India*, UNCITRAL, Final Award (Nov. 30, 2011).

⁸² *Centre for Public Interest Litigation and Others v Union of India and Others*, 2012 (3) Supreme Court cases 104.

⁸³ Forum against FDAs, *We Call Upon the Government to Review and Rescind Its Decision to Sign BIT! BIPA with the USA-Open letter to the Indian Prime Minister, Dr Manmohan Singh* (Sept. 26, 2013), available at http://www.bilaterals.org/IMG/pdf/letter-forum-agftas-us-indiabits_26-sept.pdf.

⁸⁴ Statement by P. Rajeev, Member of Parliament (India), Transcript of the Proceedings of the Rajyasabha (22 May 2012) 52-4, available at <http://164.100.47.5/newdebate/225/22052012/Full-day.pdf>.

Commerce's discussion paper 'International Investment Agreements Between India and Other Countries.'⁸⁵ The paper noted, *inter alia*, that it would be crucial for developing countries to strike a balance between investors' rights and domestic policy when entering BITs⁸⁶ and further that 'legitimate public concerns must not be subordinated to investment protection issues.'⁸⁷ The paper identified areas of concern in Indian BITs, such as the broad definition of investment, an expansive provision on expropriation without any reservations and undefined terms, in particular, fair and equitable treatment. The paper concluded by recommending a review of India's existing BITs and the striking of a balance between investor rights and the government's sovereign power to regulate in the public interest on health, safety and the environment.⁸⁸

Consequently, the above-mentioned developments paved way for India to review its BITs and critically rethink its strategy on BITs. The review revealed that India's BITs were inadequately drafted and contained vague and ambiguous provisions that could be subject to broad interpretations by arbitral tribunals.⁸⁹ India further admitted that such vague provisions were susceptible to interpretations that would encroach upon government's regulatory powers.⁹⁰ It was, therefore, imperative to adopt a new model BIT for India to reengage with its trade and investment partners. The adoption of a new model BIT was inevitable.

From the above background and the developments leading to the adoption of the model BIT, it is evident that the model BIT is an avenue for India to claw back the balance between investor rights and state's regulatory powers. For instance, on the definition of investment, the elements of indirect expropriation and the coverage of national treatment, tighter language has been introduced. Also, for the avoidance of a repeat of *White Industries* case,

⁸⁵ Ministry of Commerce, Government of India, *International Investment Agreements between India and Other Countries* [hereinafter, Commerce Ministry Paper]. As quoted in Prabhash supra n 81. It is worth noting that the paper was prepared in 2011 after the *White Industries* case. It also appears to be greatly inspired by UNCTAD's work on BITs and IIAs generally as this is quoted severally to explain various arguments. The developments taking place elsewhere on BITs such as South Africa and some Latin American countries further played a focal role in the development of the paper.

⁸⁶ *Ibid.*

⁸⁷ *Ibid.*

⁸⁸ Commerce Ministry Paper, supra 74.

⁸⁹ Government of India, Ministry of Commerce and Industry, Rajya Sabha, Question No. 1122, Answered on Jul. 26, 2017, available at <http://164.100.47.4/newsquestion/ShowQn.aspx>.

⁹⁰ *Ibid.*

where the tribunal expansively interpreted the Most Favored Nation (MFN) clause, the MFN clause has been excluded in the model BIT. The model BIT, also, excluded the umbrella clause and the Fair and Equitable Treatment (FET) clause which are considered as the catch-all phrase which investors pry on and arbitral tribunals have a field day in interpreting. Instead, the model BIT contains a provision entitled “Treatment of Investments,” thereby limiting the scope of its application.

In addition, the model BIT, quite interestingly, incorporates corporate social responsibility which requires investors to voluntarily incorporate internationally recognised standards of corporate social responsibility in their practices and internal policies. This is a plus for India and is geared towards the sustainable and equitable development of the host state.

On ISDS, the model BIT still maintains ISDS but the same is subject to the exhaustion of local remedies requirement before initiation of arbitral proceedings. However, the model BIT allows room for non-applicability of the conditions precedent if the claimant can show that there are no domestic legal remedies reasonably capable of providing any relief in respect of the same measure or similar factual matters for which a breach of treaty is claimed by the investor.

The jurisdiction of an arbitral tribunal has been significantly minimised to matters arising from only alleged breach of Chapter II of the model BIT. This chapter provides for Treatment of Investments that includes full protection and security clause, national treatment, expropriation, money transfer provisions and compensation for losses. Other limitations include, lack of jurisdiction of an arbitral tribunal to review the merits of a decision rendered by a domestic court and that a tribunal cannot accept jurisdiction over any claim that is or has been subject to arbitration under Chapter V of the treaty which provides for State-State investor settlement.

According to the Indian government, the model BIT is meant to strike a balance between protection of investments with host State’s legitimate right to regulate in the public interest and to remove ambiguity and vagueness in treaty provisions so as to limit arbitration discretion.⁹¹ A cursory look at the model

⁹¹ See Government of India, Ministry of Commerce & Industry, Department of Industrial Policy & Promotion, Lok Sabha Unstarred Question July 25, 2016), No. 1290, available at <http://164.100.47.190/loksabhaquestions/annex/9/AU1290.pdf>, accessed 24 December 2018.

BIT is sufficient to note that for India, carving out regulatory space for the exercise of the State's sovereign power to legitimately regulate in the public interest took center stage in the model BIT. This is quite understandable given the challenges of ISDS and the limitations host States have had in regulation for public interest. In addition, as noted, 'India has been long echoing the need to preserve policy autonomy in several spheres of trade policy. India has played a pivotal role in retaining policy flexibility in various areas of economic diplomacy...'⁹²

Critics have argued that the model BIT is far from attaining a balance between investor rights and the regulatory powers of the host State. They argue, if anything, the model BIT tilts the scale towards regulatory rights of the host State and significantly limits investor protections.⁹³ Further, that the model still fails considerably to delineate clear and precise treaty provisions hence giving too much leeway to arbitrators in interpretation of treaty provisions.⁹⁴

However, this observation is not accurate. Although the model BIT excludes some substantive provisions granted in traditional BITs, comparatively, it has significantly attempted to balance investor rights and the State's right to regulate in the public interest. Indeed, as further discussed below, to achieve the Sustainable Development Goals, States have to consider both sufficient guarantee of investor rights and the need for regulatory flexibility.

The Indian alternative is quite bold. While the role of BITs to influence investment inflows is debatable, for India, no doubt, they played a major role in attracting foreign investments.⁹⁵ This was mainly because foreign investors felt assured that their rights were adequately protected. However, with the new model, investment inflows have significantly reduced.⁹⁶

In conclusion, the model BIT is quite innovative and generally highlights some boundaries that India is not willing to overstep. In addition, it

⁹² James J. Nedumpara, 'India's Trade and Investment Agreements: Striking a Balance between Investor Protection Rights and Development Concerns' in Fabio Morosini and Michelle Raton Sanchez Badin (Eds), *Reconceptualizing International Investment Law from the Global South* (Cambridge: Cambridge University Press, 2018).

⁹³ Prabhash Ranjan & Pushkar Anand, *supra* n 81.

⁹⁴ *Ibid.*

⁹⁵ See Niti Bhasin and Rinku Manocha, 'Do Bilateral Investment Treaties Promote FDI Inflows? Evidence from India' (2016) 41(4) *Vikalpa: J. Decision Makers* 275.

⁹⁶ *Ibid.*

expressly limits the powers that an arbitral tribunal would normally exercise in traditional BITs, in relation to State's regulatory functions. Undoubtedly, there are criticisms against the model BIT and allegations of it being 'investor-unfriendly'. However, as observed, India seems to be ready to face such allegations head-on.⁹⁷

4.0 Conclusion

From the above discussions, it is clear that countries from the Global South are no longer willing to sit back as their sovereign rights are encroached upon by way of expansive and innovative BIT interpretations by arbitral tribunals. The legitimacy crisis, coupled with the lack of sustainability of the current ISDS regime was obviously the main crystalising factor that developing countries needed to take action and be proactive in the negotiations of investment agreements either between South-South or North-South fostering investment relations.

To take back what was given up, by way of advancing the neoliberal ideological stance which was seen as the only viable option at that time, developing countries are hands-on terminating traditional BITs and renegotiating more reasonable and balanced investment agreements. As seen, others like South Africa have opted for the domestic route in governing investment relations. Brazil was even more innovative in coming up with not only a promotion and protection of investments agreement but also one that facilitates productive investment for both the host State and the foreign investors.

Whereas, from the above, it is only India that maintains ISDS in its new model BIT, it is evident that ISDS was cautiously incorporated with significant limits on arbitral tribunals' powers in a bid to carve out regulatory space and maintain flexibility in legislation.

The neoliberal narrative on economic order that has prevailed for so many years is now facing uncertainties.⁹⁸ The Global South seems to be

⁹⁷ James J. Nedumpara, *supra* n 89.

⁹⁸ Fabio Morosini and Mitchell Ratton Sanchez Badin, 'Reconceptualizing International Investment Law from the Global South: An Introduction' in Fabio Morosini and Michelle Ratton Sanchez Badin (Eds), *Reconceptualizing International Investment Law from the Global South* (Cambridge: Cambridge University Press, 2018).

writing a new economic order which has the capability of reshaping the global economic order at large.

A paradigm shift from the competing interests of States and foreign investors to a sustainable development approach will achieve the necessary balance in ISDS. This model proposes incorporation of mechanisms that will focus on both the promotion and protection of investment without compromising on the health, security and environmental standards of the public, who in this case form a third party in investment relations. The proposed mechanisms will seek to take into account the interests of all stakeholders involved in an investment arbitration substantively and procedurally.

Depending on the context, sustainable development can mean several things.⁹⁹ This paper will adopt the United Nations' conception of right to development, which encompasses facets of the definitions of sustainable development under the environmental, human rights and economics realms.¹⁰⁰ VanDuzer et al, advance this approach and in their formulations of what constitutes sustainable development, they observe that 'economic growth is regarded as compatible with the preservation of the environment and positive social development including the alleviation of poverty in developing countries.'¹⁰¹ In this notion, development incorporates environmental protections, human health and welfare, human rights and the rights of indigenous people.

On the role of IIAs to enhance foreign investments in developing countries, scholars have argued that the signing of an IIA does not necessarily mean increased foreign investments. In fact, according to Sonarajah, studies on this issue suggest that there is little correlation between the signing of IIAs and increase in investment in-flows.¹⁰² For instance, Brazil for many years did not have any IIA in place but was extremely successful in attracting

⁹⁹ For instance, in the realm of international environmental law, it relates to the protection of the environment for the enjoyment of the present and the future generations, under human rights law it encompasses environmental sustainability, equitable development for the alienation of poverty, improved health standards, promote peace, protect human rights and pursue gender equality.

¹⁰⁰ United Nations Declaration on the Right to Development, Article 1: The right to development is an inalienable human right by virtue of which every human person and all peoples are entitled to participate in, contribute to, and enjoy economic, social, cultural and political development, in which all human rights and fundamental freedoms can be fully realized, available at <http://www.un.org/documents/ga/res/41/a41r128.htm>, accessed December 20 2018.

¹⁰¹ J Anthony VanDuzer, Penelope Simons and Graham Mayeda, *Integrating Sustainable Development into International Investment Agreements: A Guide for Developing Country Negotiators* (Commonwealth Secretariat, 2012).

¹⁰² M. Sornarajah, supra n 3.

investments.¹⁰³ However, according to investor surveys, the existence of a BIT has a positive impact on FDI flows into developing countries as this will offer investors protection, stability and predictability for FDI projects.¹⁰⁴ Nonetheless, it is acknowledged that this is only one variable in the attraction of FDI. Other factors include domestic policy environment in a State, openness to investment and trade as well as transparency.¹⁰⁵

Undoubtedly, IIAs have a significant role in the attraction of FDI in developing countries. However, the main issue is how such IIAs are drafted regarding the reciprocal obligation of investors to enhance development in host States. Therefore, the increase in FDI does not necessarily result in the automatic development of the host State, even though this was the whole point for developing countries in the race to the bottom for FDI. As Sornarajah observes, ‘liberalization of investment flows was seen as the path to development, while competing models were regarded as unsuccessful.’¹⁰⁶ There also exist competing models, being those that were based on strict regulation of the economy by the host State. He further rightly observes that states, and in particular, developing countries barely understood the repercussions of the treaties they adopted.¹⁰⁷ This position is illustrated by the boom of IIAs and the consequential investor-state disputes.

The attraction of investment is among the main agenda in the development strategies of developing countries. However, under traditional BITs, this need is seen as secondary to the protection of investors and their investments. The development of the host state is barely addressed. There is no doubt that there is need for a paradigm shift in the current status in investment treaties to address the sustainable development issues under BITs. The very recent or new era BITs recognise this deficit in the traditional BITs and incorporate certain clauses on regulation for public interest, provisions on corporate social responsibility, limitation on issues to be forwarded for arbitration and components for promotion of sustainable development for host States.¹⁰⁸ In addition,

¹⁰³ Gabriel, *supra* n 58.

¹⁰⁴ UCTAD, *The Role of International Investment Agreements in Attracting Foreign Direct Investment to Developing Countries*, UNCTAD Series on International Investment Policies for Development, 2009, available at https://unctad.org/en/Docs/diaeia20095_en.pdf.

¹⁰⁵ *Ibid.*

¹⁰⁶ M.Sornarajah, *supra* n 3.

¹⁰⁷ *Ibid.*

¹⁰⁸ EU-Canada Comprehensive Economic and Trade Agreement (CETA), EU-Singapore, Canada-China 2012 BIT, Indian Model BIT, US 2012 Model.

the vagueness and ambiguity of provisions is being cured by delineating clear and precise definitions of terms.

The notion of sustainable development in ISDS encompasses elements and mechanisms that can be incorporated into ISDS which will not only achieve a fundamental balance between investor rights and the sovereign powers of the State to regulate in the public interest, but also take into account the interests of the crucial 3rd party: the public, in terms of sufficient representation and participation in ISDS. To achieve this goal, efforts should be made on several dimensions. The first dimension, which should also cover the substantive aspect of ISDS is on the initial stage of treaty negotiating and drafting. This stage also includes involvement of the public through active consultation: ensuring transparency and consistency. The other dimension to look at are the procedural aspect of ISDS, which will include the role of the tribunal in enhancing legitimacy in ISDS and the overall balance between investor protection and regulation in the public interest. This aspect will also include mechanisms of inclusion and representation of the public in ISDS and avenues of instilling confidence in arbitrators in ISDS.

These aspects are discussed below in detail.

4.1.0 The Initial Stage and the Substantive Aspects of ISDS

This stage mainly focuses on the incorporation of a sustainable development approach in IIAs and consequently in ISDS. At this stage, it is imperative that the host State is proactive in both treaty negotiation and drafting. In negotiations, the host State has to understand the nature of its obligations and at the same time carve out space for regulatory flexibility.

In order to achieve this delicate balance in ISDS, IIA negotiations and drafting should be clear on the rights and the obligations of both parties. In particular, in order to achieve a sustainable development approach in ISDS, IIAs should be drafted with both protection of investment and promotion of sustainable development of the host State in mind. This can be achieved through, delineating clear and precise definitions of terms to minimise the expansive interpretations by arbitral tribunals, express provision on matters an arbitral tribunal can exercise jurisdiction and most importantly carve out space for legislative flexibility which can be done through clarification of scope and meaning of treaty provisions and by using specific flexibility mechanisms

such as exceptions and reservations.¹⁰⁹ Further, States can shield themselves against unjustified liability and high procedural costs through treaty design by looking into options on how dispute settlement is conducted and in the scope and application of treaty clauses.¹¹⁰

On dispute settlement, an IIA can set out preconditions on ISDS. For instance, exhaustion of domestic judicial systems within the host State, the use of other Alternative Dispute Resolution (ADR) mechanisms that can be utilised prior to institution of ISDS as a last resort and exploit other innovative mechanisms, such as, opting for State-State arbitrations for matters arising out of pre-establishments rights provisions, qualifying consent to ISDS and providing for the possibility of counter-claims by States.¹¹¹

On the other hand, to ensure protection of investors, IIAs should provide express provisions on compensation for expropriation. As Giovanni notes, in the presence of an express provision on compensation for an expropriation, States are bound by such clauses and thus cannot disregard an obligation voluntarily assumed.¹¹²

4.2.0 Procedural Aspects of ISDS

To fully enmesh a sustainable development approach in ISDS, the procedural aspects of ISDS too have to be reformed. This goal can be achieved through several avenues as discussed below.

4.2.1.0 Legitimacy Enhancements

Essentially, these are mechanisms adopted by a tribunal to alleviate pressure from critics and at the same time strengthen the legitimacy of ISDS.¹¹³ Arbitral tribunals are seen to be embracing this nuanced approach in a bid to enhance their legitimacy. For instance, in the recent *Philip Morris decision*,¹¹⁴

¹⁰⁹ UNCTAD Investment Policy for Sustainable Development, 2015, available at https://unctad.org/en/PublicationsLibrary/diaepcb2015d5_en.pdf, accessed 6 May 2019.

¹¹⁰ Ibid.

¹¹¹ Ibid.

¹¹² Giovanni, *supra* n 18.

¹¹³ See generally, Annalisa M. Leibold, 'The Friction Between Investor Protection and Human Rights: Lessons from *Foresti v South Africa*' [2015] *Houston Journal of International Law*, Forthcoming, available at <https://ssrn.com/abstract=2586252>, accessed 20 April 2019.

¹¹⁴ *Philip Morris Brands Sàrl, Philip Morris Products S.A. and Abal Hermanos S.A. v Oriental Republic of Uruguay*, ICSID Case No. ARB/10/7.

the tribunal took into consideration the so-called non-commercial values¹¹⁵ in an attempt to strike a balance between State obligations and investor rights. In this case, the tribunal found that the government measures in issue, had been adopted bona fides for the purpose of protecting public welfare, were non-discriminatory and were proportionate. That they were not to be considered as an expropriation and, therefore, the Claimants did not have any right to compensation despite the negative effect on their business.¹¹⁶

This tendency of legitimacy enhancement by tribunals is further observed in various other awards¹¹⁷ including, the *Foresti case*¹¹⁸ where the tribunal allowed for further ‘Non-Disputing Party’ participation and shifted costs to the Claimant due to the friction generated from a case in which an investor’s rights directly conflicted with a state’s right to enact positive human rights legislation.¹¹⁹ Another way an arbitral tribunal can enhance its legitimacy can be by taking into account investor behaviour when settling investor-state disputes.¹²⁰ This inclination by tribunals is commendable and a significant step towards the revival of legitimacy in ISDS.

4.2.2.0 Public Participation

Participation of the members of the public in matters that have significant social and economic impact on them is another limb of sustainable development. As VanDuzer et al observe, to ensure sustainable development through international investment rules, ‘they should be developed through wide consultation with people in the host country and decisions about the negotiation, application and interpretation of agreements should be transparent and consistent.’¹²¹ This participation extrapolates to dispute settlement too. Members of the public are a significant stakeholder in ISDS as taxpayers.

¹¹⁵ Giovanni supra n 18, non-commercial values as those “not pertaining to the protection of property but relating to the safeguard of other essential interests such as environment and human health” also see Mary E. Footer, ‘Bits And Pieces: Social And Environmental Protection In The Regulation of Foreign Investment’ (2009) 18(1) Michigan State Journal of International Law, 33.

¹¹⁶ Ibid at para 305.

¹¹⁷ *Methanex Corporation v United States of America*, NAFTA/UCITRAL Award, 03/08/2005, *Chemtura Corporation v Government of Canada*, NAFTA/UNCITRAL Award, 02/08/2010, *Philip Morris Brands Sàrl, Philip Morris Products S.A. and Abal Hermanos S.A. v Oriental Republic of Uruguay*, ICSID Case No. ARB/10/7.

¹¹⁸ *Foresti case*, supra n 43

¹¹⁹ Ibid.

¹²⁰ UNCTAD, supra n 105.

¹²¹ Vanduzer et al., supra n 98.

This participation can be achieved through *amicus* submissions. *Amicus* participation has several advantages: aids in the protection of public interests, enhances transparency, improves the quality of the award and enhances public scrutiny of the process.¹²²

In the current ISDS regime, *amicus* briefs are a rarity.¹²³ It has been argued that there is an inherent conflict in the ICSID Rules on the admissibility of *amicus* briefs.¹²⁴ However, as observed, *amicus* briefs are now becoming a significant player in matters involving important public policy considerations.¹²⁵ In fact, in the recent case of *Achmea v Slovak*,¹²⁶ which is deemed as a significant milestone in ISDS history on *amici* briefs, the *amicus* submissions were made at the invitation of the tribunal.¹²⁷

4.2.3.0 Transparency

It is acknowledged that arbitration as an alternative dispute settlement mechanism is a private process between a claimant and a respondent. However, in the context of ISDS, the respondent is a State and the implications of the process are inevitably extended to the public. Transparency in this respect can be enhanced through making available/public documents¹²⁸ related to the dispute, public access to the hearing and as mentioned above admission of *amicus* submissions.

New era BITs seem keen on incorporating transparency-related clauses. For instance, the 2012 U.S BIT model contains provisions titled “Transparency of Arbitral Proceedings”,¹²⁹ Comprehensive Economic and Trade Agreement

¹²² Manjiao Chi, *Integrating Sustainable Development in International Investment Law: Normative Incompatibility, System Integration and Governance Implications*, (Routledge, 2017) 123.

¹²³ Emmert and Esenkulova *supra* n 14.

¹²⁴ Ibid, “On the one hand, Rule 37(2)(a) requires that “the non-disputing party submission would assist the Tribunal in the determination of a factual or legal issue related to the proceeding by bringing a perspective, particular knowledge or insight that is *different* from that of the disputing parties”. On the other hand, unless the disputing parties give broad consent, the non-disputing party will have very limited rights and even more limited access. But how are the *amici* supposed to know what they might be able to add beyond what is already presented to the tribunal by the disputing parties, if they do not have access to the files?”.

¹²⁵ Ibid.

¹²⁶ Manjiao Chi, Ibid at 122.

¹²⁷ Ibid.

¹²⁸ These can include pleadings and submissions filed by the parties, submissions of non-disputing parties, procedural decisions, arbitral award and records of the hearing.

¹²⁹ 2012 U.S. Model BIT.

(CETA) adopts UNCITRAL Transparency Rules;¹³⁰ and in the Canada-China BIT, an arbitral tribunal has no power to decide whether hearings should be made public and that decision is left to the disputing State subject to consultation with the disputing investor.¹³¹

4.2.4.0 Reform of Arbitration Rules

These reforms should be aimed at revision of institutional rules governing international arbitrations to curb the problem of inconsistency in decisions arising out of ISDS. Such revisions are such that will allow more transparency of arbitral proceedings and can include an establishment of review bodies to permit review of investment treaty awards.¹³² It has been suggested that this option is more practical and has a chance of being established efficiently compared to seeking amendment of treaties which can be cumbersome and less effective.¹³³ The reforms suggested include establishment of working groups from different backgrounds drawn from arbitration practitioners, international lawyers, former government officials, among others to establish a uniform code of best practices for ISDS that would take into account the inherent uniqueness of ISDS and public implications of investment treaty arbitrations. Best practices can include, heightening or allowing transparency of arbitration proceedings through publication of awards and access to documentation in ISDS especially in matters that generate public interest and revision of cost-shifting rules to give tribunals clearer guidance on when it would be appropriate to shift costs to discourage institution of unmeritorious claims.¹³⁴

However, the establishment of these protocols would require instigation of political will to revise or supplement the current rules.¹³⁵ For instance, for ICSID Rules, there could be constraints arising from the ICSID Convention which may prove to be a real barrier to reform in this area.

¹³⁰ EU-Canada Comprehensive Economic and Trade Agreement.

¹³¹ Canada-China BIT as quoted in Manjiao Chi, *supra* n 117 at 123.

¹³² Nigel Blackaby, Public Interest and Investment Treaty Arbitration, in *International Commercial Arbitration: Important Contemporary Questions* (Albert Jan van den Berg ed., 2002) as quoted in Susan D. Frank, 'The Legitimacy Crisis in Investment Arbitration: Privatizing Public International Law Through Inconsistent Decisions' (2005) 73 *Fordham Law Review* 1521.

¹³³ Susan D. Frank, *supra* n 127.

¹³⁴ *Ibid.*

¹³⁵ *Ibid.*

ISDS is the main form of dispute resolution platform relied upon by parties in investment treaties as it is perceived to offer a neutral and impartial forum for resolving disputes between States and foreign investors. However, the regime is currently facing a legitimacy crisis due to the mounting criticisms ranging from inconsistencies in decisions, costs of arbitration and even credibility of arbitrators. In addition, the inherent structural imbalance of BITs heavily undermines ISDS from playing a more constructive role in investment governance.

Mechanisms must be incorporated to strike a balance between promotion and protection of investment and the sovereign right of the State to regulate in the public interest. A paradigm shift to a sustainable development approach in ISDS taking into account the rights of all stakeholders involved in investment arbitration is the most promising avenue to revive its legitimacy. As noted, '[d]eveloping states have to change their traditional passive stance and participate positively in international investment policy making, and make their great efforts and contributions as pioneers for the initiative and development of BIT practice with their developing and developed counterparts.'¹³⁶

¹³⁶ Zeng Huaqun, 'Balance, Sustainable Development, Integration: Innovative Path for BIT Practice' (2014) 17 *Journal of International Economic Law*, 299.